

25 Years After the Asian Financial Crisis: What Have We Learned

Hoe Ee Khor, Chief Economist

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Outline of Presentation

- Causes of the crisis
- Lessons of the crisis
- Reforms of the policy and regulatory framework at the individual country level
- Reforms of the international financial architecture
- New risks and challenges
- Future direction

Once Upon a Time in Asia: Headline News Back in 1997

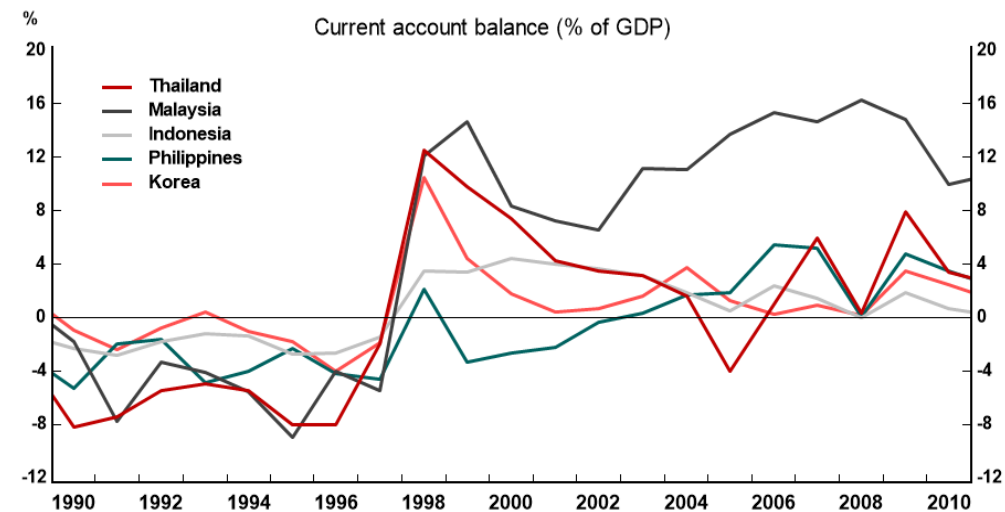
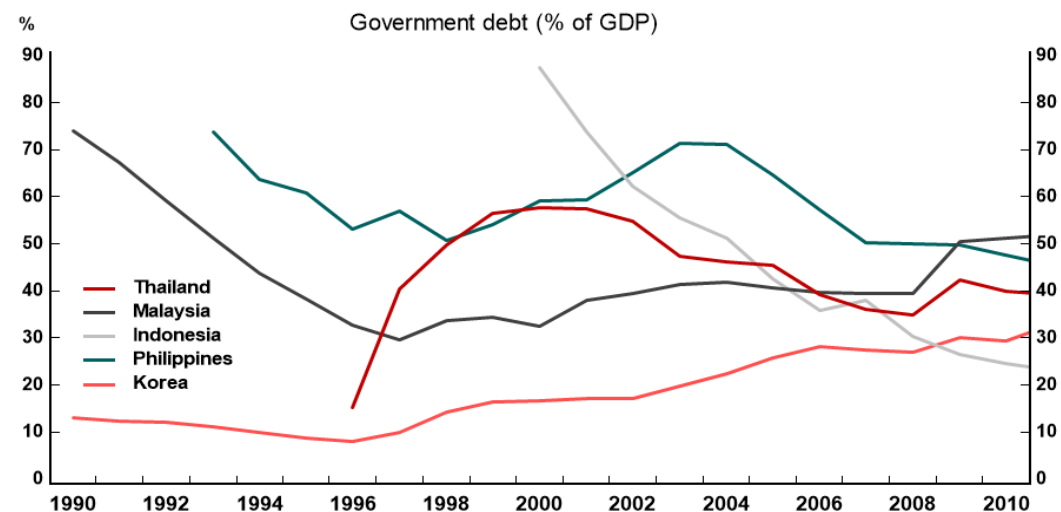
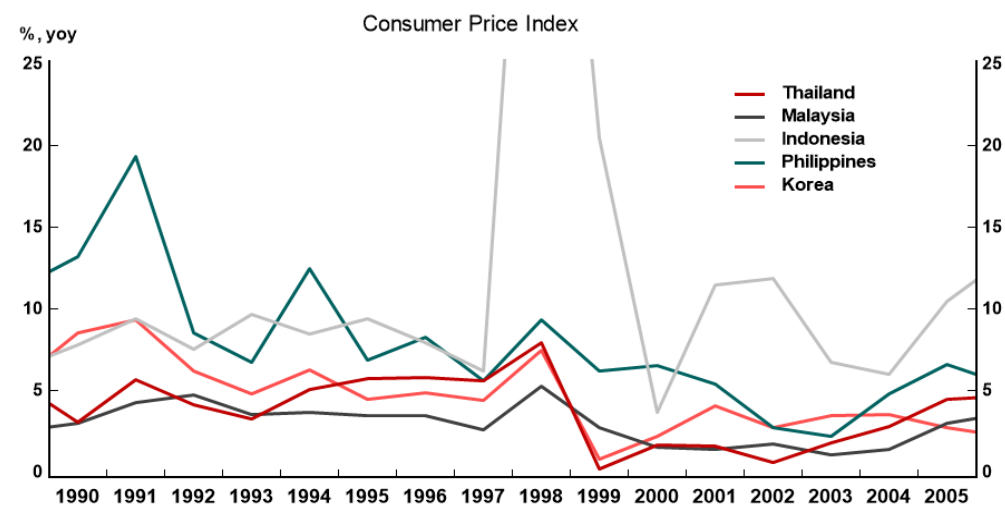
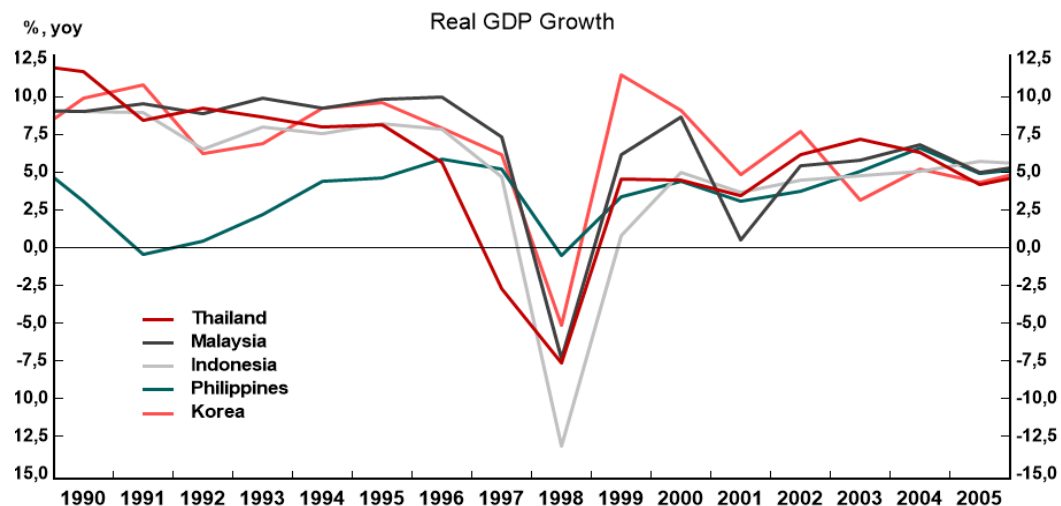
- **“Thai Stocks Tumble as Baht Slides to Weakest in a Decade” (May 14, 1997)**
- “Soros Led Attack on Baht, Says Thai Central Banker” (June 24)
- “Thai Currency Reserves Drop to \$33.3 Bln After Baht Defense” (June 26)
- “IMF, Japan, Others to Lend Thailand \$16 Billion” (Aug 12)
- “Thailand Closes 56 Finance Companies, Two to Reopen” (Dec 8)
- **“Indonesia Floats the Rupiah; Currency Sinks 5%” (Aug 15, 1997)**
- “Indonesia’s Soedradjad Asks Banks to Cut Loans to Importers” (Aug 15)
- “Indonesia in Talks with IMF on Rupiah Collapse” (Oct 8)
- **“Get out of Korea, Right Now!” (Nov 5, 1997; Peregrine Securities Report)**
- “Korean President Apologizes to Nation for Seeking IMF Bailout” (Nov 22)
- “IMF Approves \$3.58 Bn Installment for South Korea” (Dec 19)
- “Korea, Thailand, Indonesia Ratings Cut to Junk by Moody’s” (Dec 22)
- **“Greenspan Blames Asian Policies for Currency Crisis” (Oct 14, 1997)**
- “IMF’s Camdessus Says Asian Fund Will Fail if IMF Impaired” (Nov 13)
- “Asia Bailout Fund Evolves toward Cooperative Facility” (Nov 18)



A South Korean labor union member of Seoul Bank, one of South Korea's most bad-debt burdened commercial banks, looks downcast. (Source: US Federal Reserve History)

<https://www.federalreservehistory.org/essays/asian-financial-crisis>

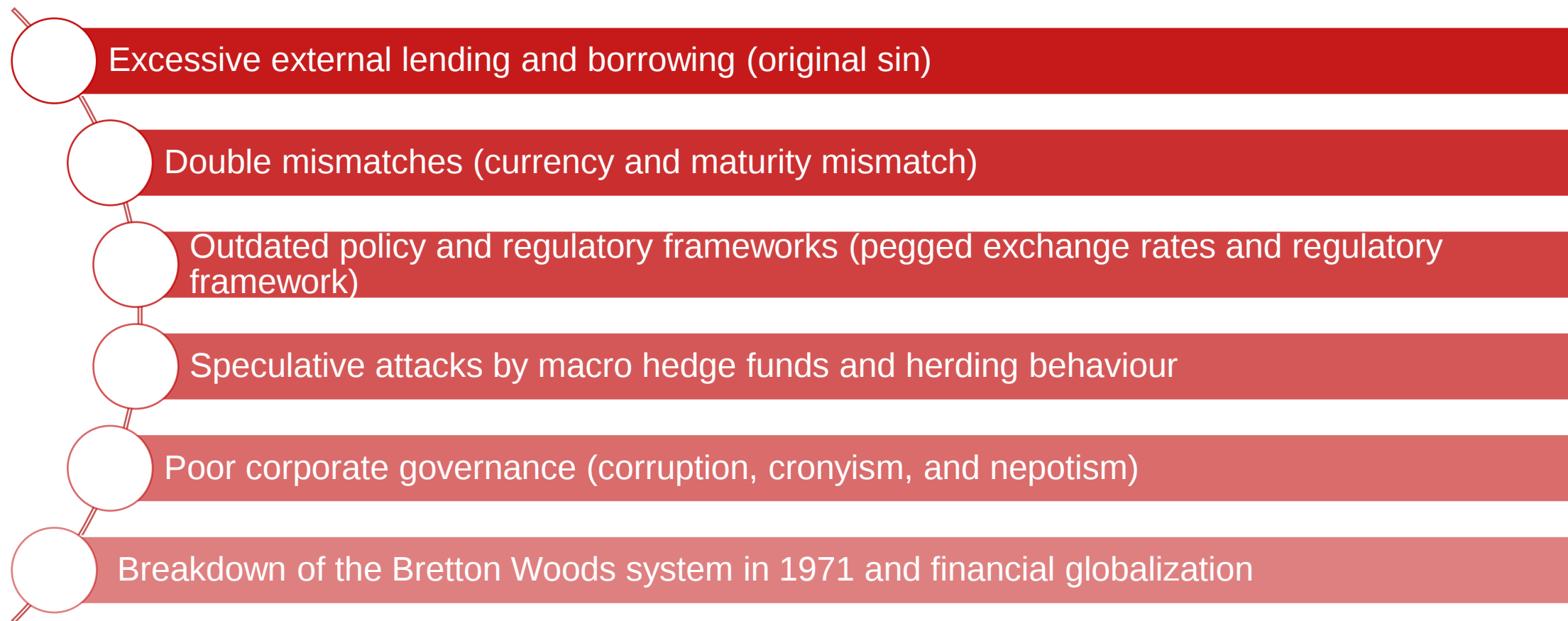
ASEAN-4 and Korea: “Strong Fundamentals” prior to the AFC



Source: IMF and Haver Analytics
Note: ASEAN-4 comprises Indonesia, Malaysia, Philippines, and Thailand. Data on public debt ratio are included when available.

Causes of the Asian Financial Crisis (1)

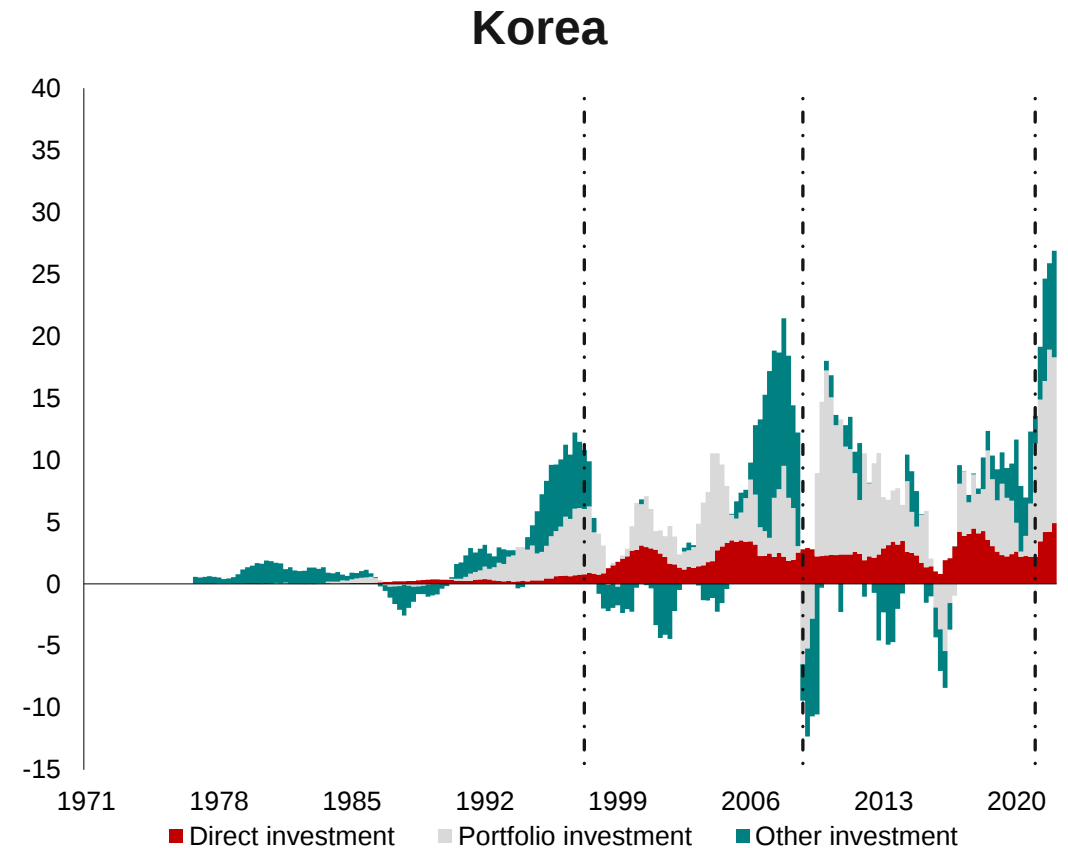
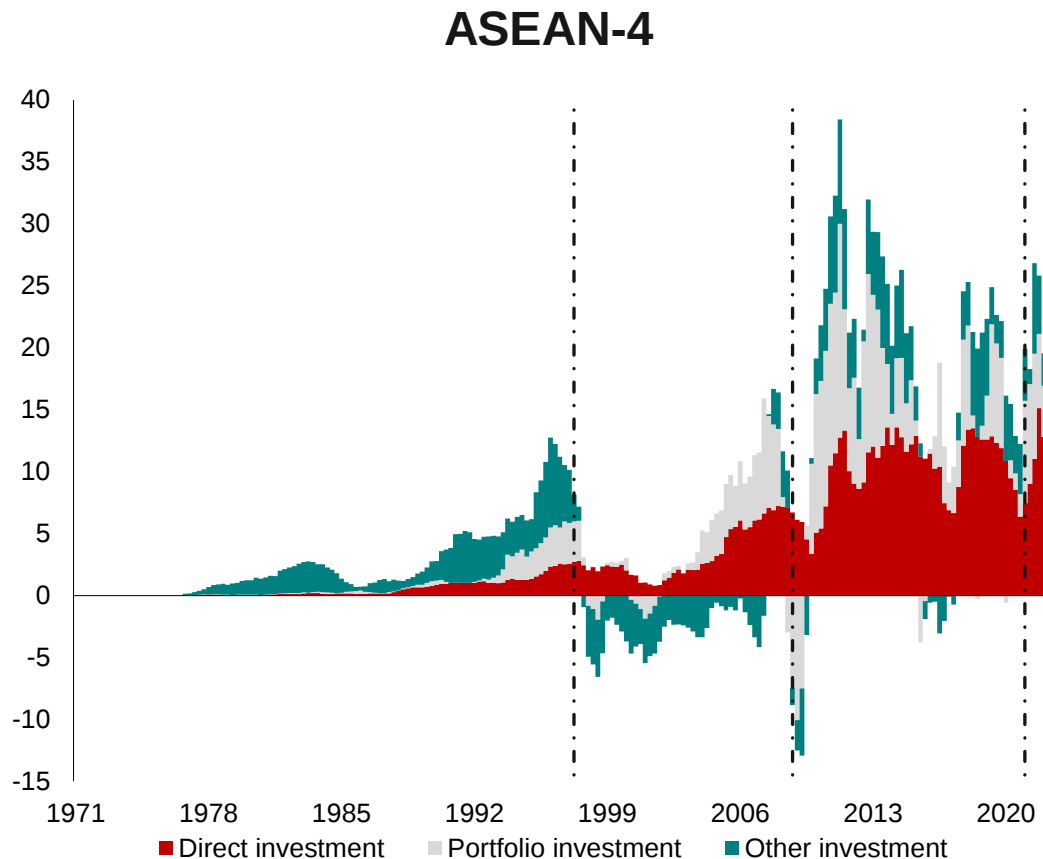
The AFC was mainly caused by a combination of macroeconomic imbalances, external developments, and structural weakness in the financial and corporate sectors...



Causes of the Asian Financial Crisis (2)

... amplified by sharp reversals in capital flows and market confidence (sudden stop).

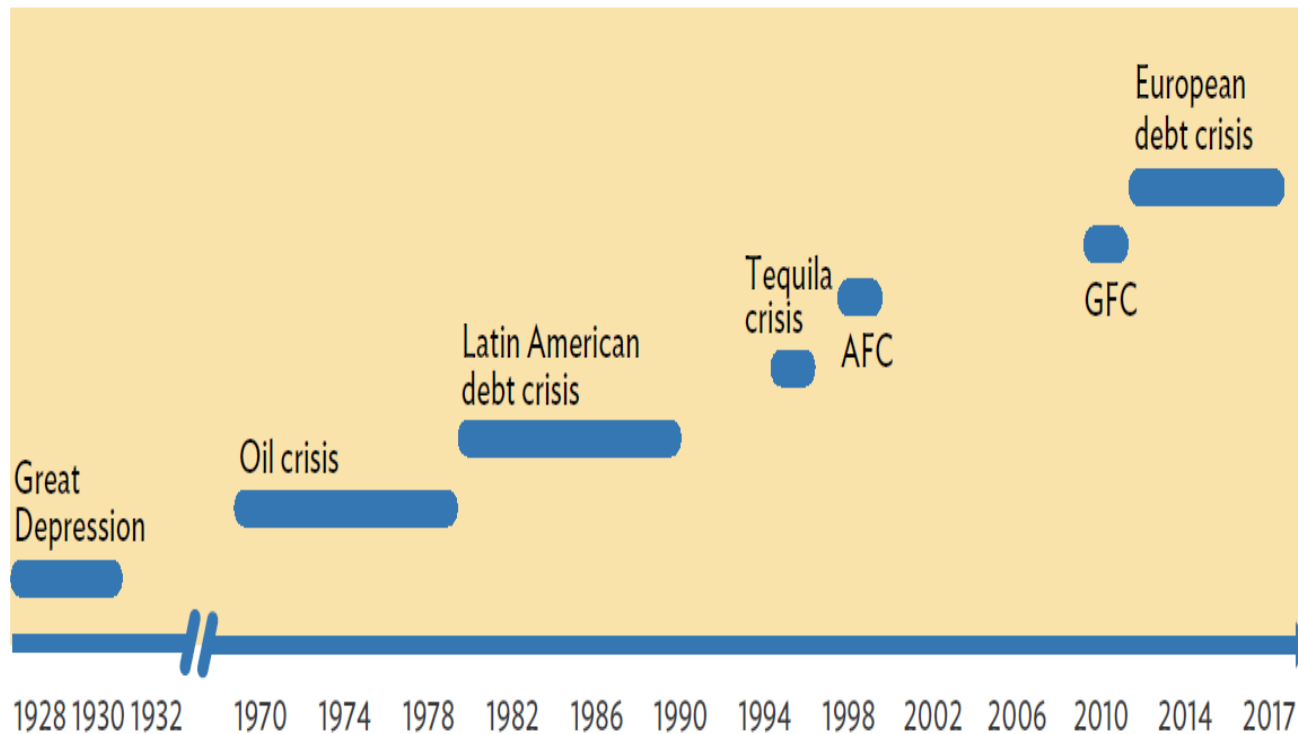
Selected ASEAN+3: Non-Resident Capital Flows (USD billion, 4-quarter moving average)



Causes of the Asian Financial Crisis (3)

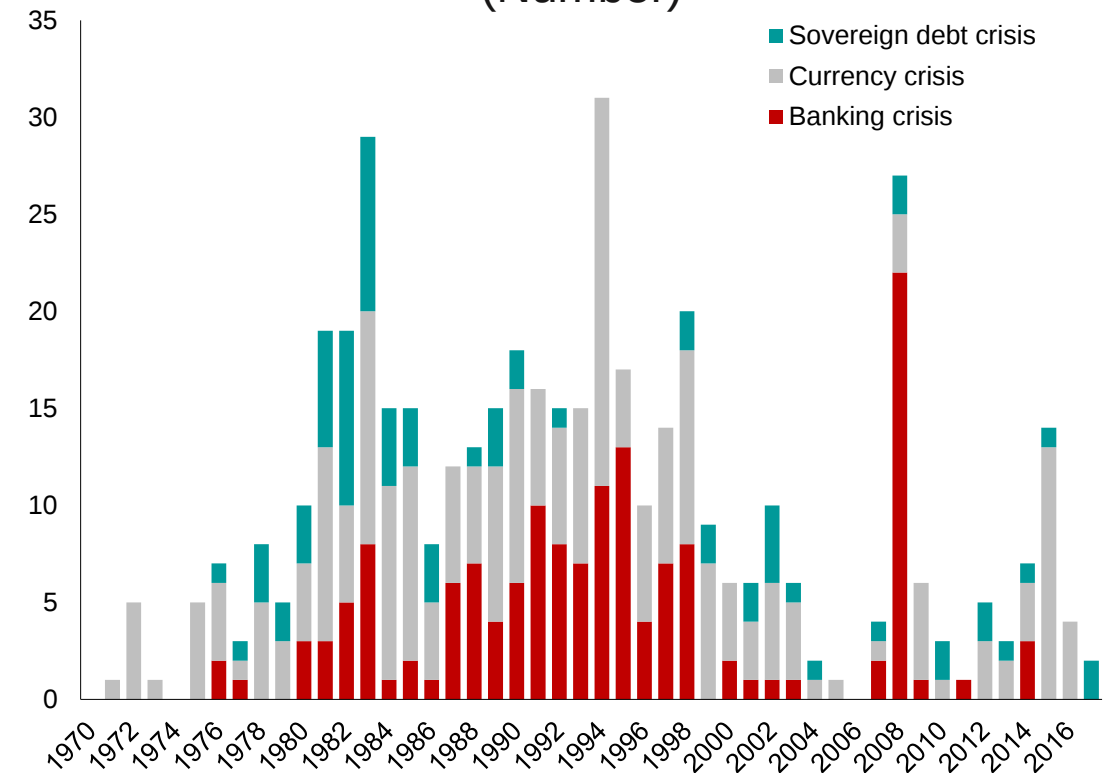
The poorly planned financial liberalization and premature capital account opening since the breakup of the Bretton Woods System in the early 1970s also contributed to the build-up of debt vulnerabilities in EMEs.

Chronology of Financial Crises



Source: ADB

Frequency of Financial Crises (Number)



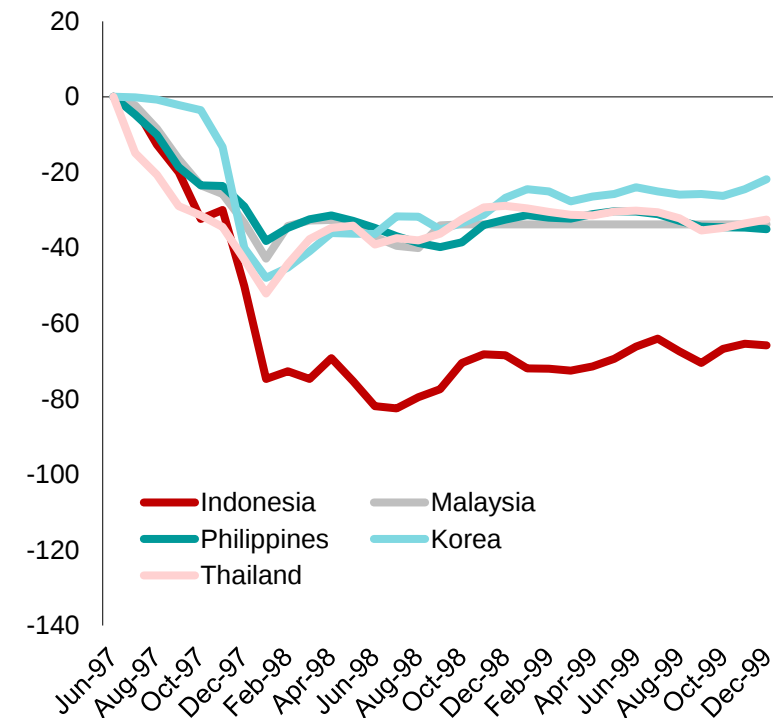
Source: Laeven and Valencia (2018) "Systemic Banking Crises Revisited".

Costs and scarring effects of the Asian Financial Crisis (1)

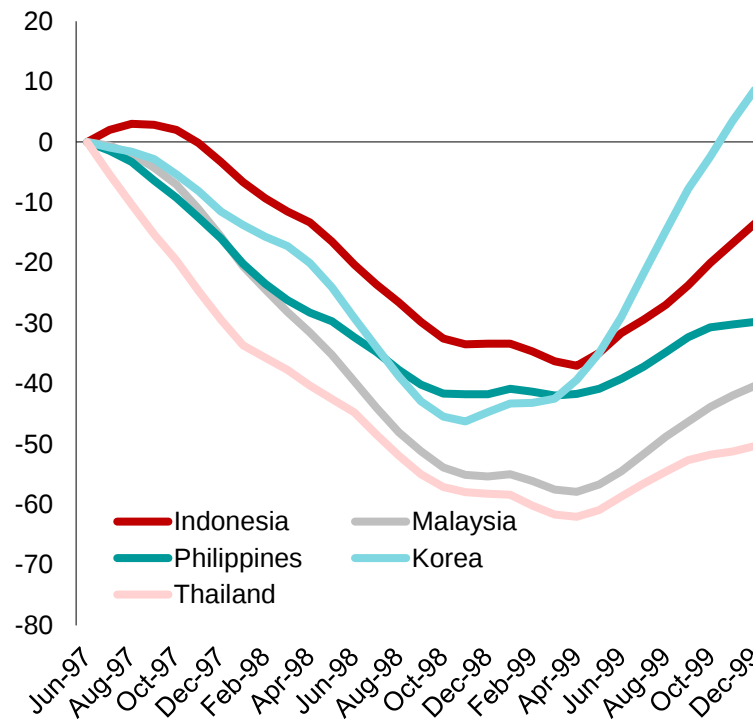
The AFC immediately triggered a sharp currency depreciation, a loss in investor confidence, and economic contraction.

Sudden Stop Contagion (Cumulative percent change from June 1997)

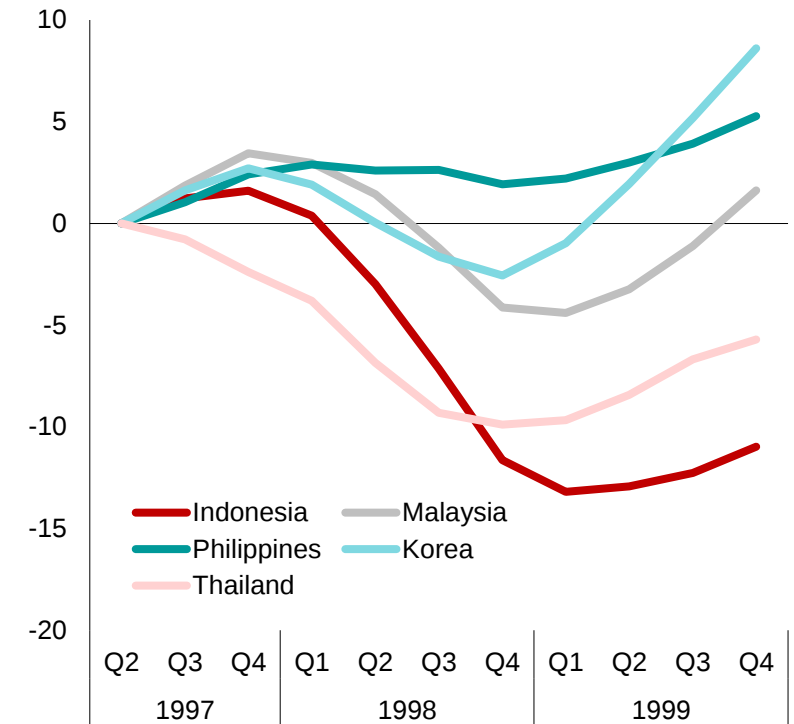
Currency



Stocks

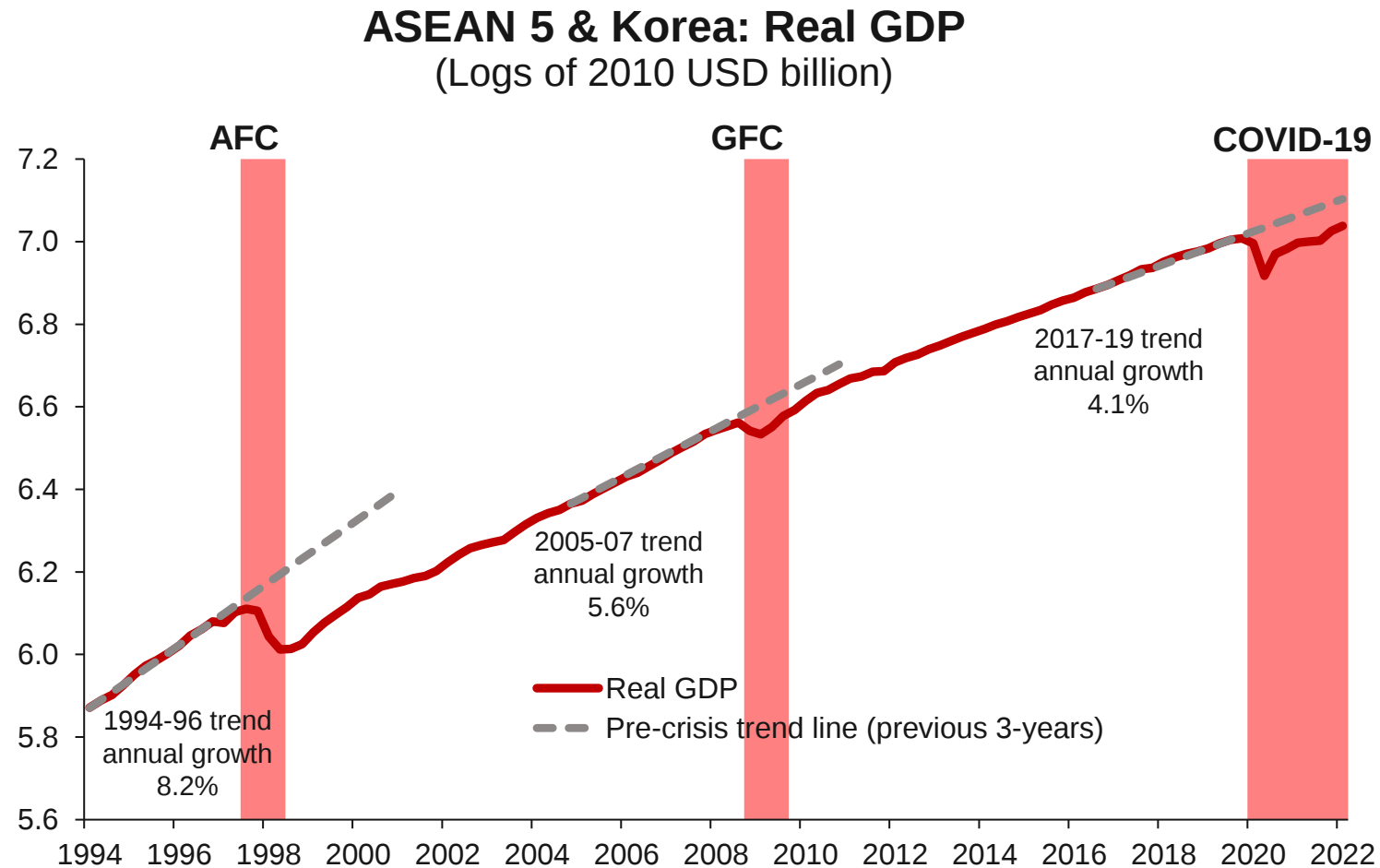


Real GDP



Costs and scarring effects of the Asian Financial Crisis (2)

while threatening the region's long-term economic growth.

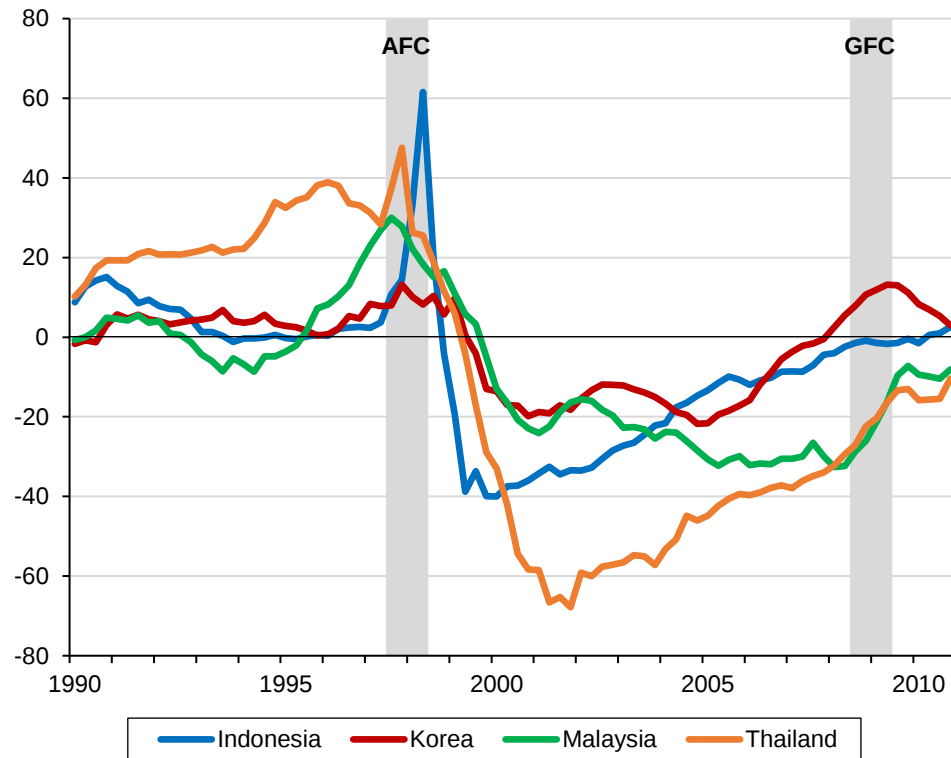


Sources: National authorities via Haver Analytics; and AMRO staff calculations.
Note: Note: 'ASEAN 5' includes the original 5 members: Malaysia, Indonesia, Philippines, Singapore and Thailand.

Costs and scarring effects of the Asian Financial Crisis (3)

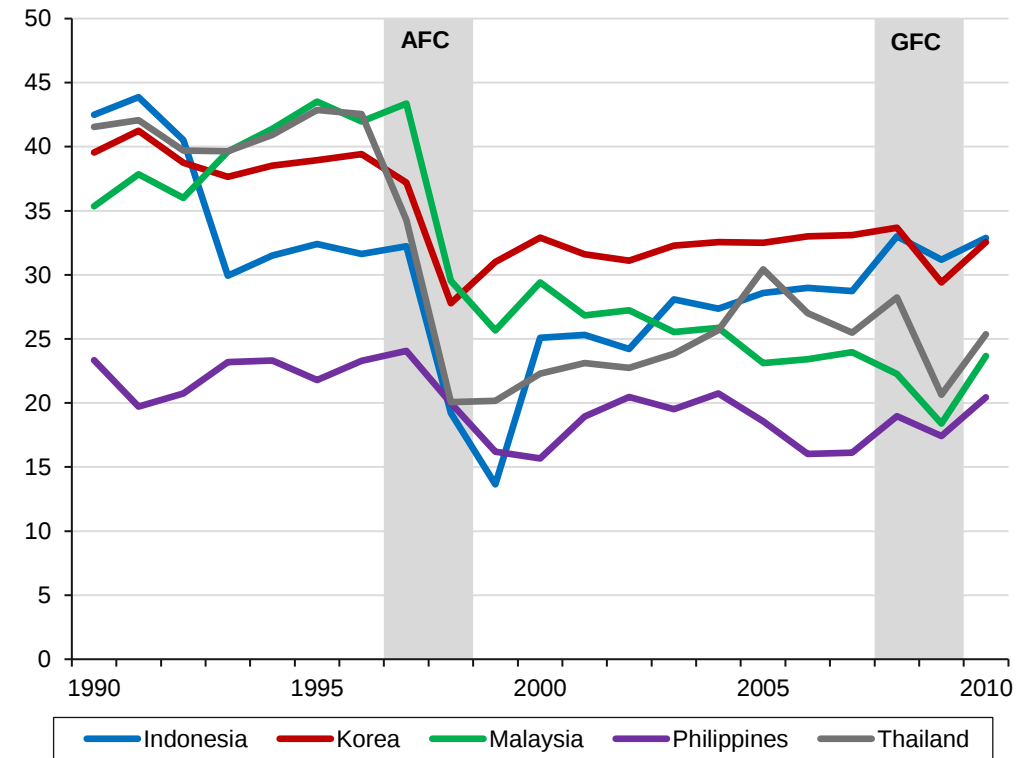
The crisis-hit countries were forced to go through a long period of deleveraging and the collapse of investment.

**Credit-to-GDP Gaps
(Percent of GDP)**



AFC = Asian financial crisis, GDP = gross domestic product, GFC = global financial crisis.
Source: Bank for International Settlements.

**Domestic Investment
(Percent of GDP)**

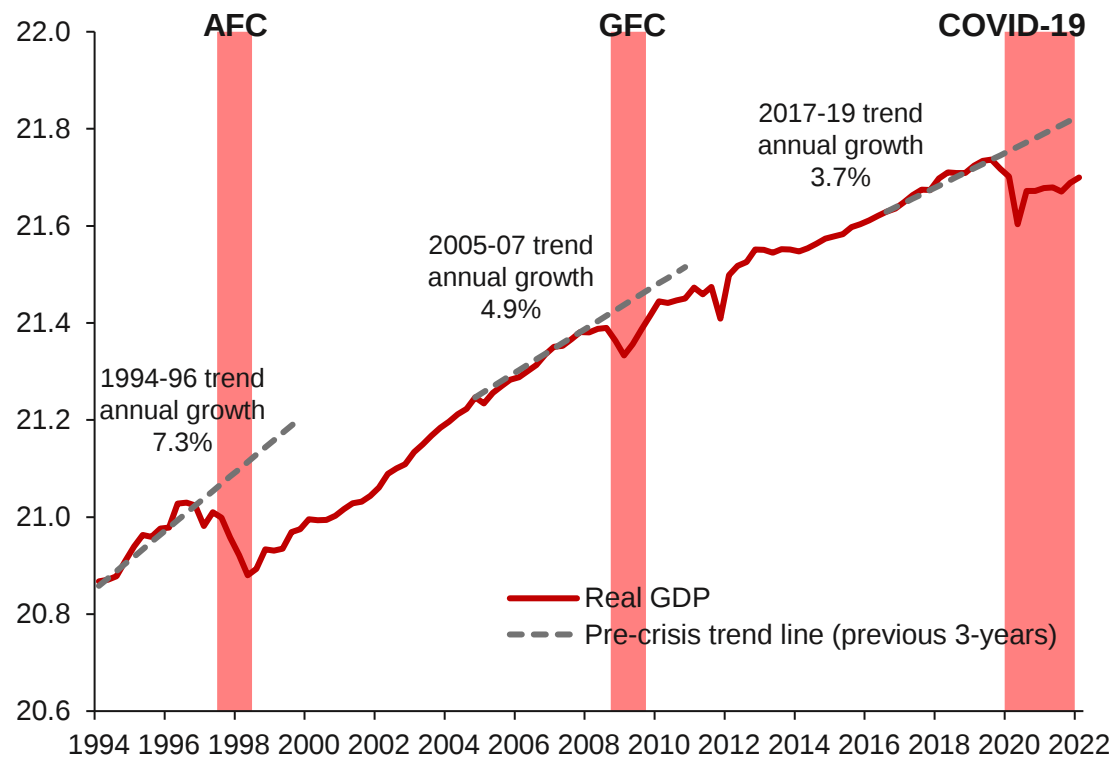


AFC = Asian financial crisis, GDP = gross domestic product, GFC = global financial crisis.
Source: International Monetary Fund.

Country case (1): Thailand

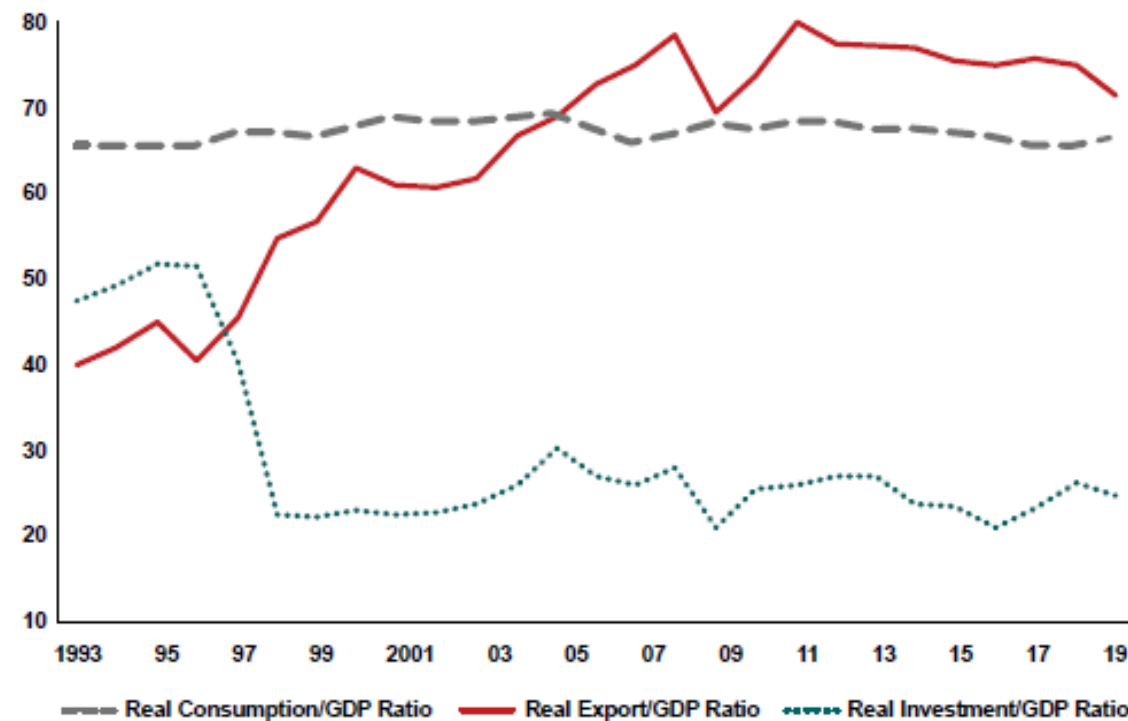
With the corporate sector's debt restructuring, investment declined substantially from the pre-crisis level, and contributed little to the post-crisis recovery.

Thailand: Real GDP
(Logs of THB million)



Sources: National authorities via Haver Analytics; and AMRO staff calculations..

Thailand: Post-Crisis Changes in Growth Driver
(Percent of GDP)

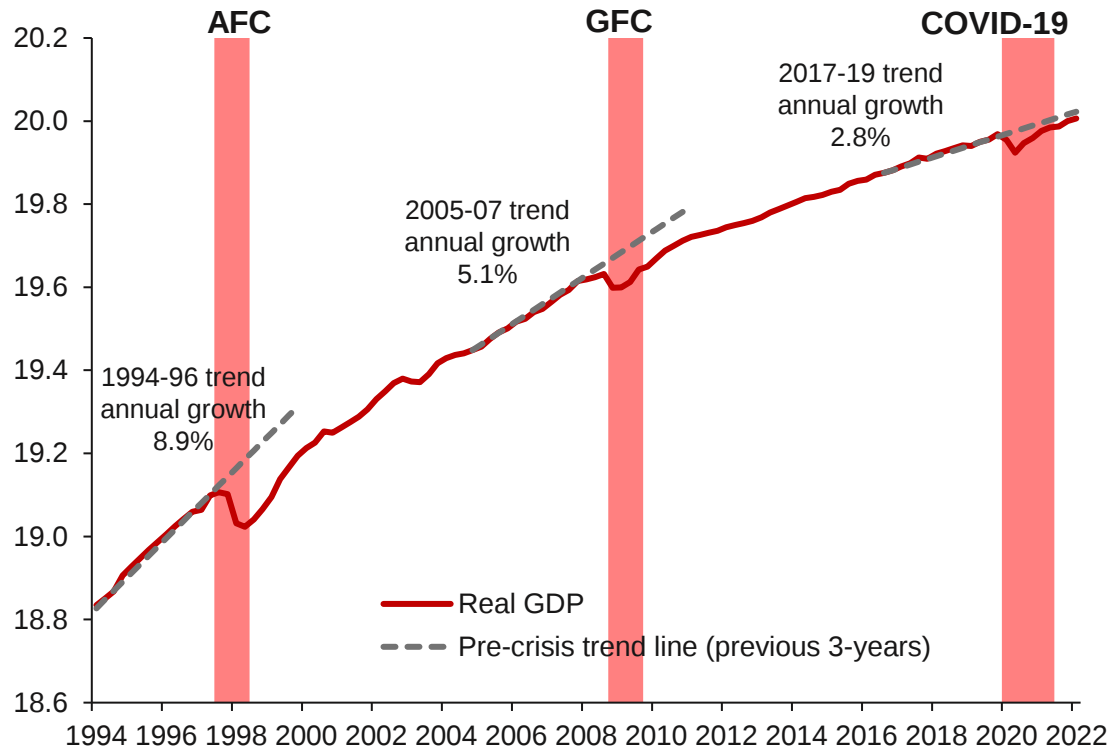


Source: National Economic and Social Development Board; Chalongsob (2022) Chapter 14, "Trauma to Triumph – Rising from the Ashes of The Asian Financial Crisis"

Country case (2): Korea

Chaebols' investment booms in 1994-1996, led by excessive leverage, was normalized with drastic debt restructuring and financial sector reforms in the post-AFC period.

Korea: Real GDP
(Logs of KRW million)



Sources: National authorities via Haver Analytics; and AMRO staff calculations..

Korea: Private Investment and Corporate Credit
(Percent of GDP)

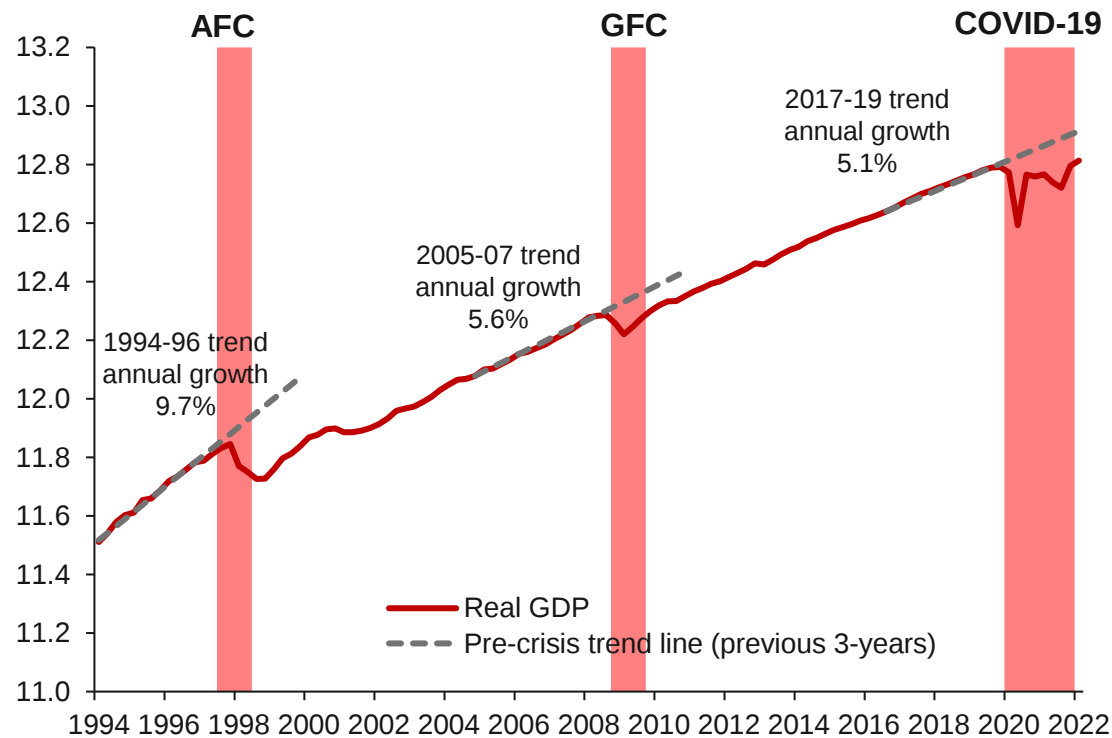


Source: Bank of Korea; Hahm and Kim (2022) Chapter 17, "Trauma to Triumph – Rising from the Ashes of The Asian Financial Crisis"

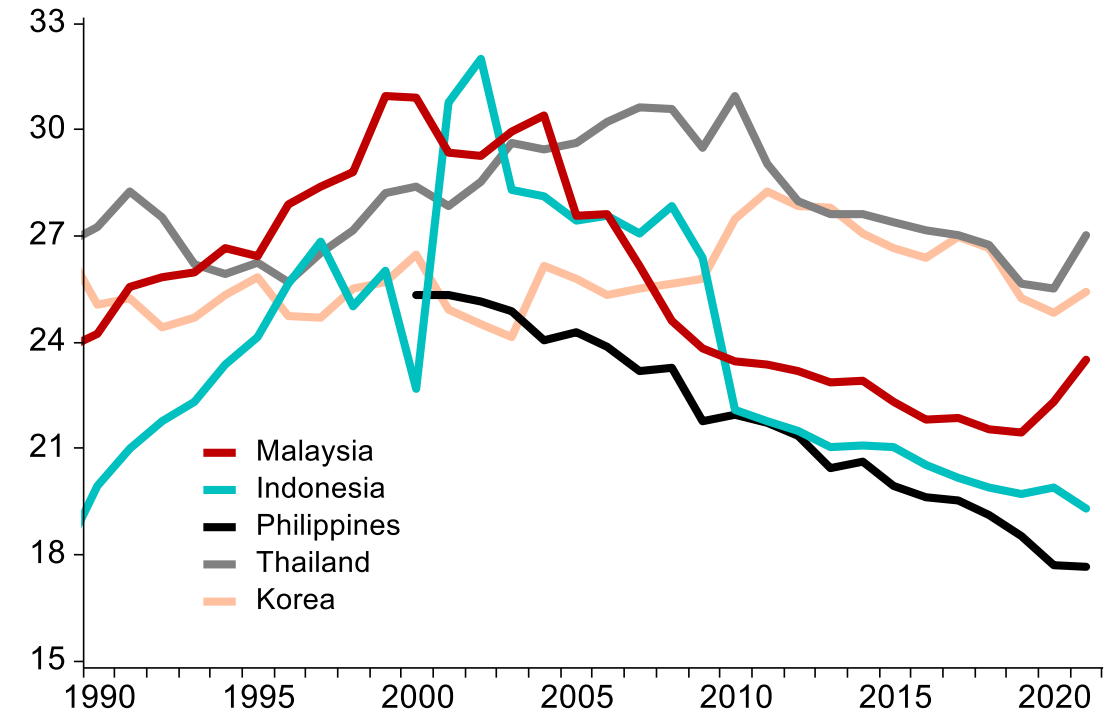
Country case (3): Malaysia

After the AFC, the decline in the manufacturing sector and exports led to the economy's greater dependence on the services sector and domestic demand, partly explaining a shift to a lower level of economic growth.

Malaysia: Real GDP
(Logs of MYR million)



Crisis-hit Economies: Manufacturing Share of GDP
(Percent of GDP)



Sources: National authorities via Haver Analytics; and AMRO staff calculations..

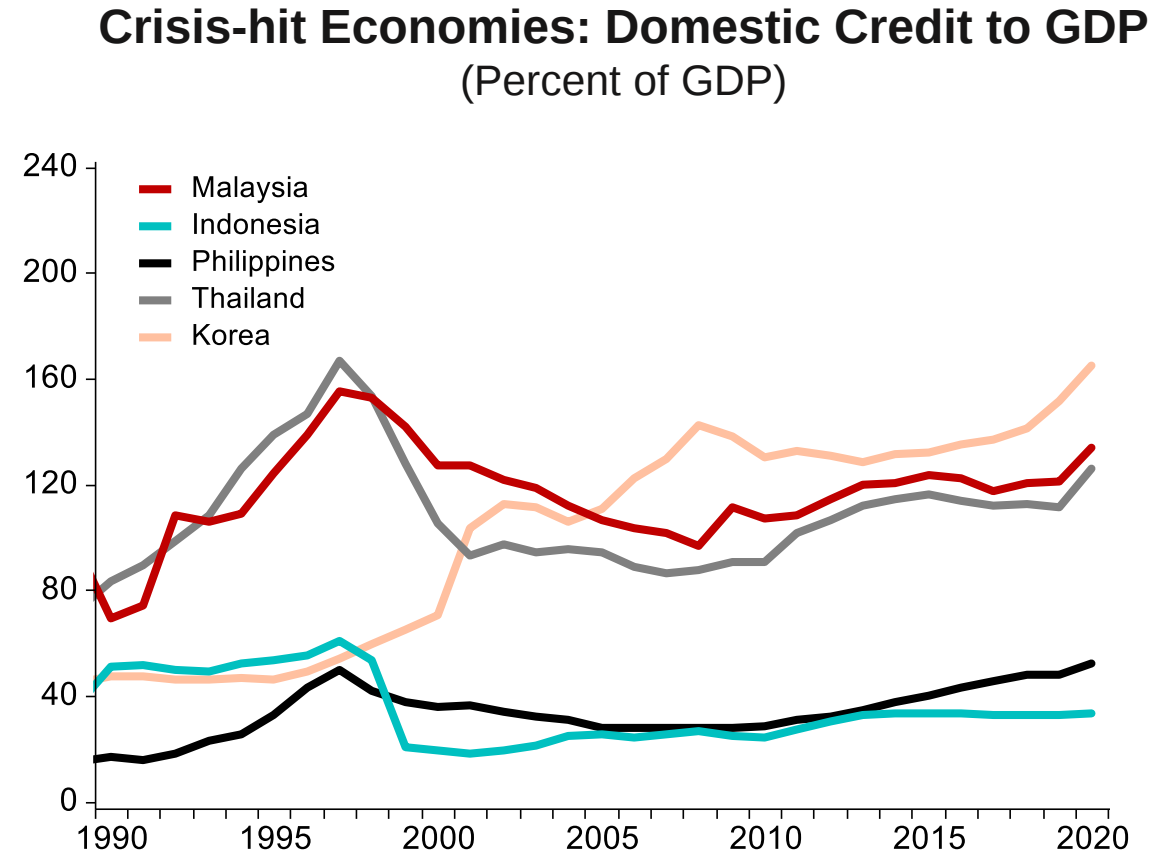
Source: World Bank via Haver Analytics

Country case (4): Indonesia

The growth of credit and investment tumbled due to the restrictive macroeconomic policy, a disconnect between monetary policy and real sector, and the lure of higher returns from investing in financial assets.



Sources: National authorities via Haver Analytics; and AMRO staff calculations..



Source: World Bank via Haver Analytics

Lessons from the Asian Financial Crisis (1)

Handling Economic Challenges

Key lessons from the AFC

- Policymakers should pay more attention to the dynamics of **cross-border capital flows** and **global financial markets**
- **Exchange rate** should be more flexible and supported by ample reserves and policy buffers

Enhanced macro-financial policy framework

- More disciplined **monetary policy framework**
- **Fiscal consolidation** to establish fiscal discipline
- Strengthening of **the financial regulatory framework**
- **Better prudential oversight** to deal with financial stability risks

Strengthened economic fundamentals

- **Economic growth momentum** regained
- **Financial health** restored by repairing the balance sheets of corporates and banks
- **Deleveraged and rebuilt fiscal space**
- **External position** strengthened with a significant build-up in FX reserves

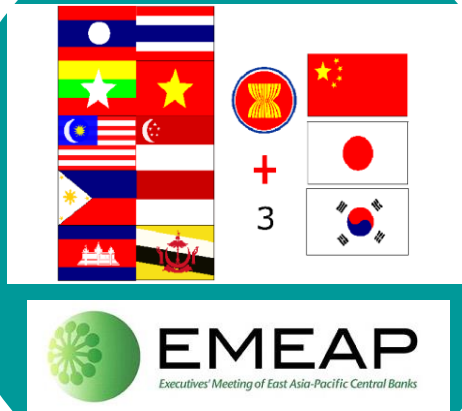
Lessons from the Asian Financial Crisis (2)

Launching Regional Financial Cooperation

Strengthening
Financial
Safety Net

Upgrading
Economic and
Financial
Surveillance

Financial Market
Development

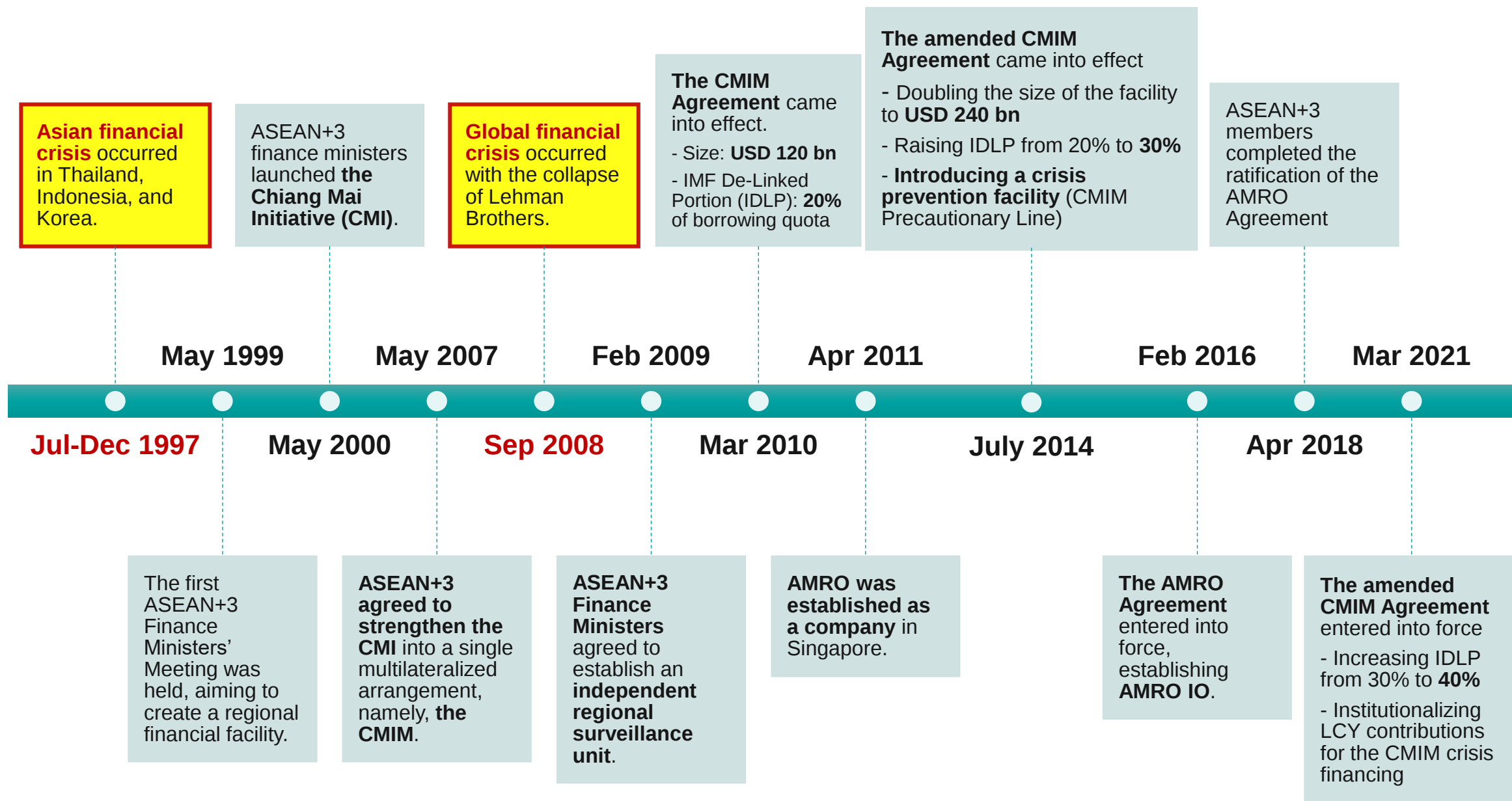


- Launch of **the CMI** at the ASEAN+3 FM Meeting (2000)
- **Upgraded to the CMIM** (2010), **CMIM-SF** totaling USD 120 billion (2010) and **CMIM-PL** doubling the size of the facility to USD 240 billion (2014)
- **The IMF-delink portion raised** from the initial 10% to 40% (2021)

- Launch of **the Economic Review and Policy Dialogue (ERPD)** process (May 2000)
- Establishment of **AMRO** as regional surveillance arm of the CMIM (Apr 2011)
- **AMRO's official designation as an IO** (Feb 2016)

- Launch of the **Asian Bond Markets Initiative (ABMI)** (Aug 2003)
- Creation of the **Asian Bond Funds (ABF)** under the initiative of EMEAP (Jun 2003)

Timeline of the Regional Financial Cooperation



Expanding ASEAN+3 Bilateral Swap Agreements (BSAs)

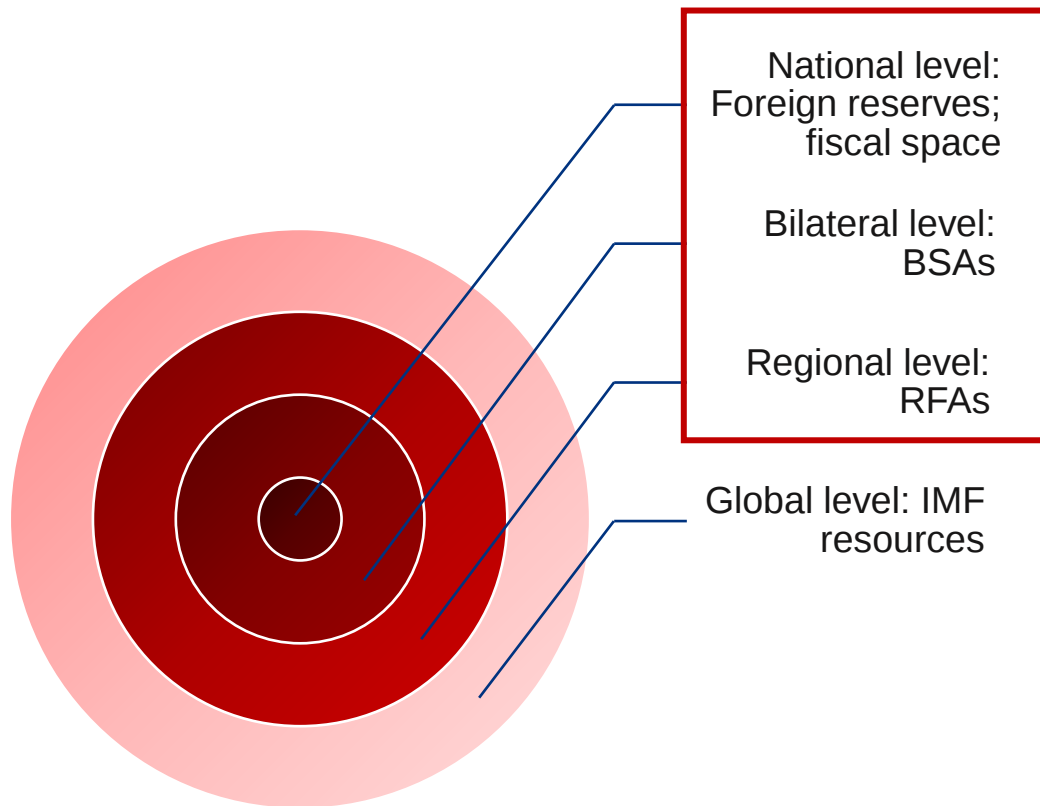
Year	Amount (USD bn)	PBC- BNM	PBC- MAS	PBC- BOT	PBC- BI	PBC- HKMA	PBC- BOK	PBC- BOL	PBC- BOJ	PBC- BSP	JMOF- BI	JMOF- BSP	JMOF- BOT	JMOF- BNM	JMOF- MAS	BOJ- MAS	BOJ- BOT	BOK- BI	BOK- BSP	BOK- BNM	BI- MAS	BI- BNM
2009	82.0	•			•	•	•															
2010	108.4	•	•		•	•	•			•									•			
2011	168.7	•	•		•	•	•															
2012	188.6	•	•		•	•	•															
2013	222.5	•	•		•	•	•														•	
2014	175.2	•	•	•	•	•	•														•	
2015	171.4	•	•	•	•	•	•														•	
2016	172.2	•	•	•	•	•	•									•					•	
2017	250.3	•	•	•	•	•	•					•	•	•		•		•			•	
2018	333.0	•	•	•	•	•	•		•		•	•	•	•	•	•		•			•	•
2019	323.7	•	•	•	•	•	•		•		•	•	•	•	•	•		•			•	•
2020	352.6	•	•	•	•	•	•	•	•		•	•	•	•	•	•	•	•			•	•
2021	371.6	•	•	•	•	•	•	•	•		•	•	•	•	•	•	•	•			•	•
2022	382.2	•	•	•	•	•	•	•	•		•	•	•	•	•	•	•	•			•	•

Sources: national authorities' website, as of March 2022; AMRO staff calculations

Lessons from the Asian Financial Crisis (3)

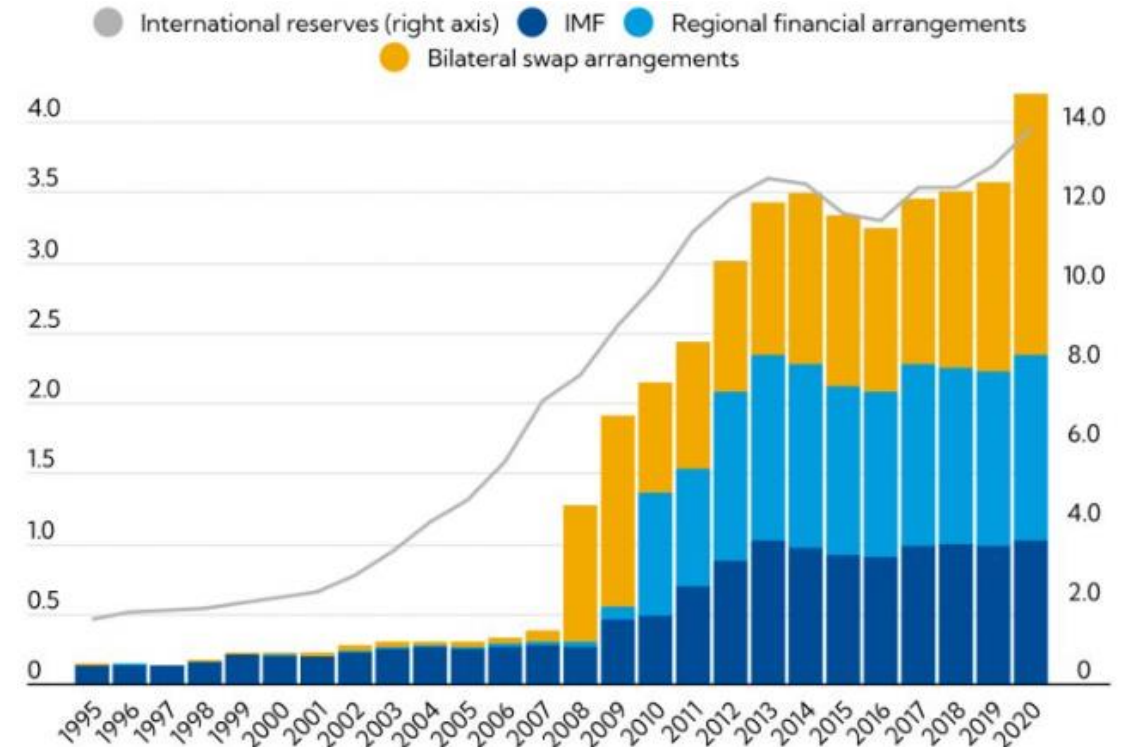
Sizing Up the Global Financial Safety Net

Schematic of the Global Financial Safety Net



Sources: ESM; IMF; and AMRO staff illustration.

Evolution of Global Financial Safety Net (USD trillions)



Sources: M. Perks, Y. Rao, J. Shin, and K. Tokuoka (2021); US Federal Reserve website; RFA annual reports and press releases; and IMF staff calculations. For details see IMF Special Series note on COVID-19 "The Global Financial Safety Net during the COVID-19 Crisis: an Interim Stock-Take." Note: Since the safety net is comprised of different currencies, its USD value fluctuates with exchange rate changes.

Lessons from the Asian Financial Crisis (4)

Strengthening the international financial cooperation

Setting Up the Financial Stability Forum

- In October 1998, the **Group of Seven (G7)** financial authorities held the first meeting.
- The **Financial Stability Forum (FSF)** and the **Group of Twenty (G20)** were set up in February and September 1999, respectively.
- Clearly recognized the need to strengthen **regulatory and supervisory measures** for highly leveraged hedge funds, offshore markets, and short-term capital flows

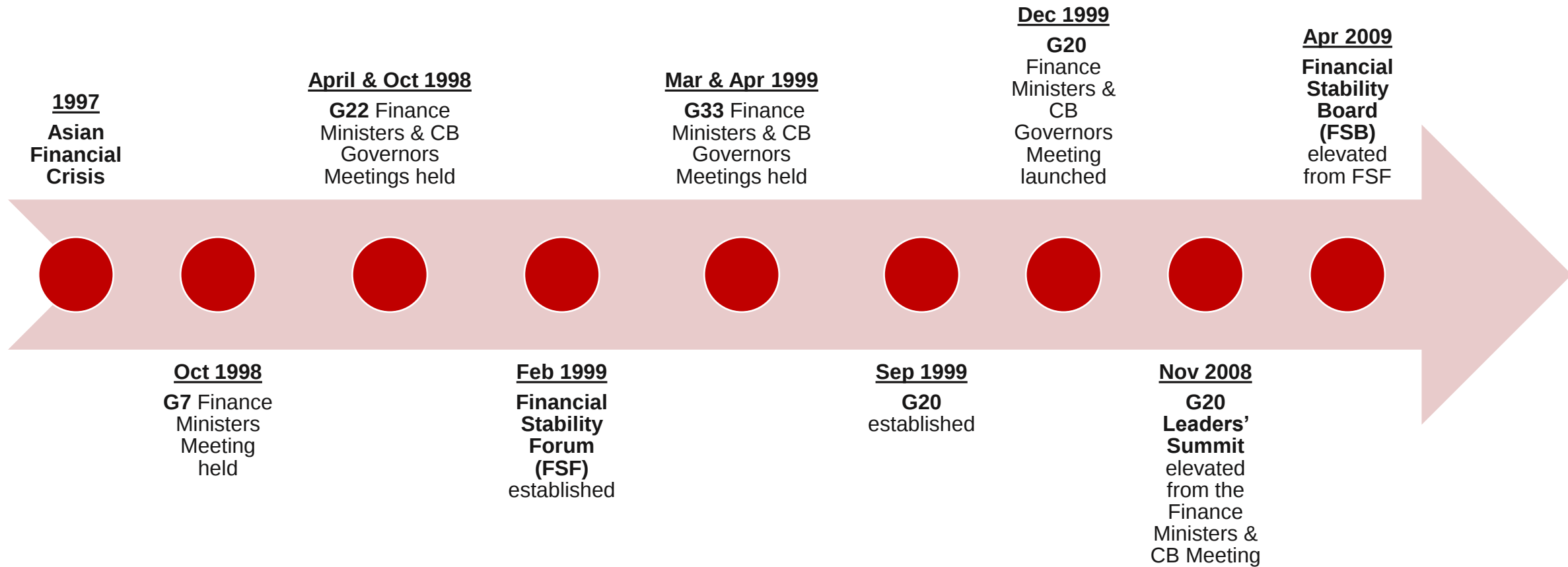
Group of Twenty (G20)

- The **G20** elevated to **Leaders' summit level** from Finance Ministers/Governors in November 2008.
- Elevated the **FSF** to the **Financial Stability Board (FSB)** in April 2009
- Issued principles for cooperation between **the IMF and RFAs**

The IMF Reforms

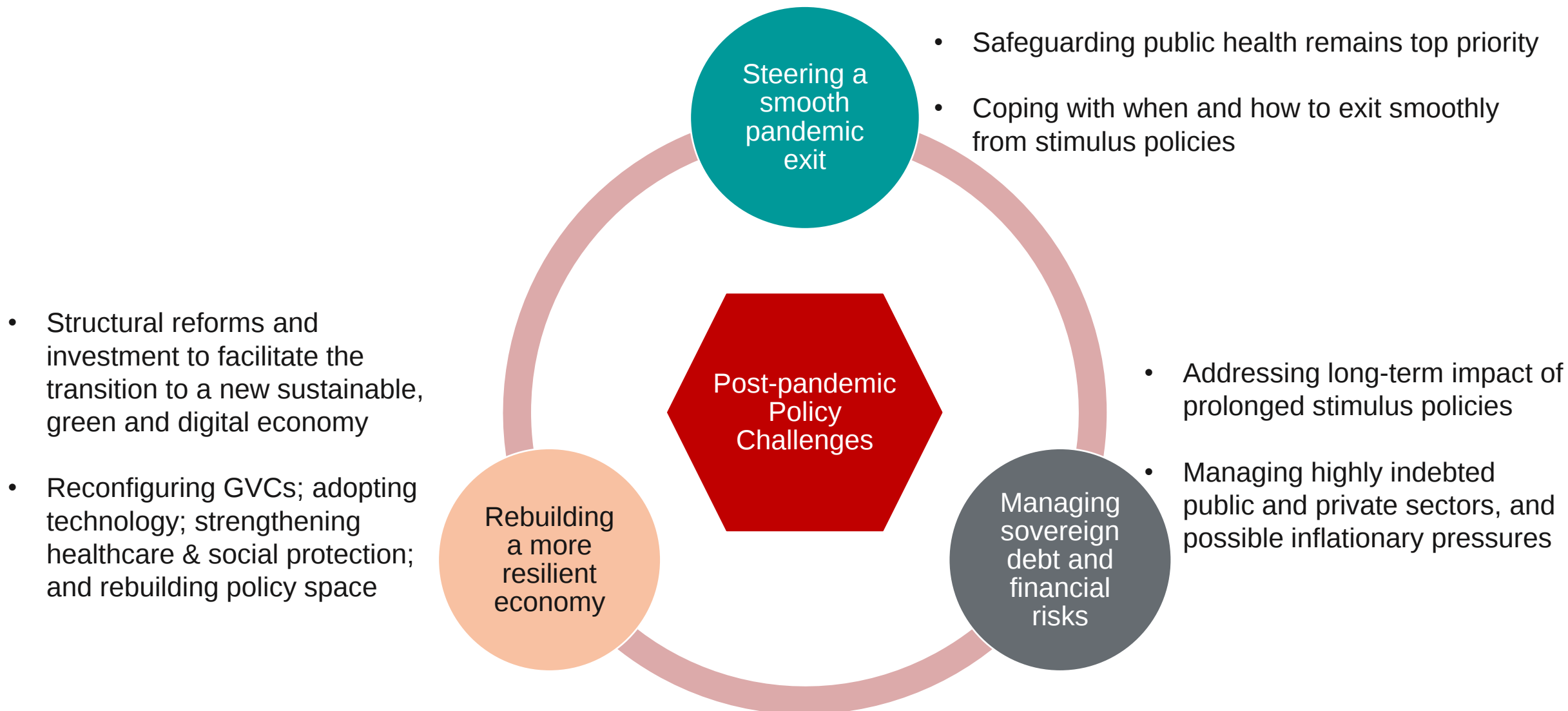
- Conducted **surveillance** reforms (e.g. IMF FSAP 1999 and International Capital Markets Dept 2001)
- Streamlining **structural conditionality**
- Formalizing cooperation with **regional financing arrangements**
- Use of **capital control**

Timeline on the Evolution of FSF and G20



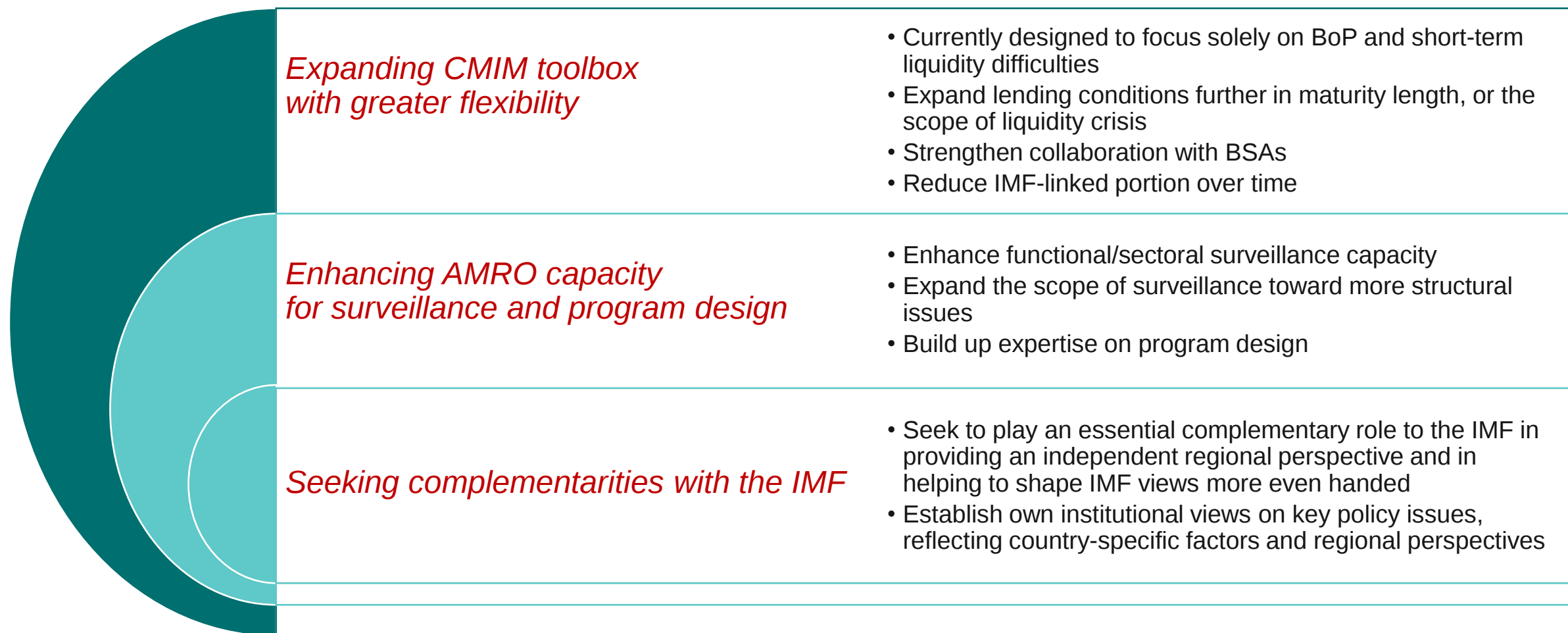
New Risks and Challenges (1)

Transitioning to the endemic and boosting structural reforms



New Risks and Challenges (2)

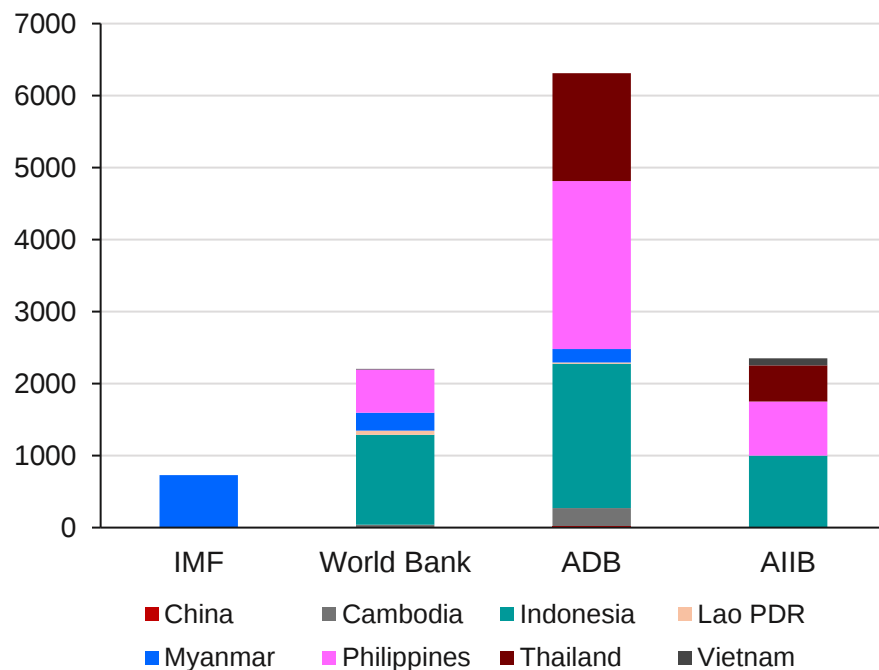
The outbreak of the COVID-19 pandemic highlights the need for broadening the AMRO's mandate to cope with structural issues, such as climate change, and growing demand for longer term finance.



New Risks and Challenges (3)

Beyond the CMIM: Coping with Longer-term Financing Needs

Financial Assistance from IMF and MDBs to ASEAN+3 during COVID-19 Pandemic
(In millions of USD)



Source: IMF, World Bank, ADB and AIIB websites; AMRO staff calculations (as of 9 September 2020, except for Myanmar as of 6 May 2021; as the calculation method is different in each institution, the validity of the quoted amounts is subject to further confirmation)

Growing needs for long-term financing during the pandemic

- Most financing has come from MDBs to assist ASEAN+3 members in development, structural reforms and budget support.

CMIM's focus on short-term BoP liquidity crisis

- The current mandate of the CMIM may be too narrow to cover the needs for longer-term financing.

Exploring alternative ways to support longer-term financing needs in the region

- AMRO to increase capacity to provide TA for low-income countries
- Closer cooperation between the CMIM/AMRO and the ADB
- ASEAN+3 members may consider ramping up the current framework of regional financial cooperation toward strengthening long-term financing support

Thank you



Contact Us

Add: 10 Shenton Way, #15-08/9, Singapore 079117

Tel: +65 6323 9844

Email: khhor.hoeeee@amro-asia.org

Website: www.amro-asia.org